

an adequate revenue stream from its pay-per-view and information offerings over its half of the Cerritos system, it should nevertheless bear all of the residual risks.

The three adjustments we identified are:

1. "Nonrecoverable costs". The tariff materials do not specify precisely what costs are supposedly nonrecoverable. GTE has not adequately explained its inclusion of "nonrecoverable costs." However, "nonrecoverable" costs are not generally used in standard ratemaking practice by GTE or other LECs, and certainly do not apply to a situation where a customer makes an up-front lump-sum payment. GTE's entire support for the "nonrecoverable" cost consists of the following verbal explanation unsupported by any workpapers or calculations:

[A]nnual nonrecoverable cost reflects a portion of the investment and labor cost which must be recovered over the revenue life. The Nonrecoverable costs are derived by computing an annuity for the present value of capital investment plus income tax effects, based upon the revenue life of the service and a discount rate equal to the authorized rate of return for local exchange carriers. Depreciation, return and tax expenses were then subtracted from the annuity amount to arrive at the total nonrecoverable cost."¹²

This explanation is not sufficient to replicate the annuity calculation used by GTE. However, the annual "nonrecoverable cost," \$303,784, represents an annuity payment that would recover any undepreciated plant at the end of the 12 year service life and all of the gross investment adjustment that is shown on Exhibit A to Transmittal 873.¹³

The annual depreciation charges shown on Exhibit B to Transmittals 873 and 874 will not fully recover some \$2.4 million of the initial net book investment of \$5,948,981. This conditions is typical of tariffed service offerings. The service life of an individual LEC

¹² Transmittal 873 D&J, p. 11.

¹³ Different methods exist to calculate an annuity. The formula we used was $PV = (1/r) - (1/(r(1+r)^t))$, for t-years (12) and r interest rate (11.25%). Brealey and Meyers, Principles of Corporate Finance, (Fourth Edition), 1991.

service usually is less than the total productive life of the assets used to provide such a service. Most of the \$2.4 million remaining net plant balance likely represents unrecovered investment in conduit plant. Conduit investment represents about \$3.099 million, or 52% of the total system investment.¹⁴ The service life is 12 years. GTECA's current prescribed remaining life for regulated conduit investment is 41.1 years.¹⁵ Therefore, a substantial amount of the conduit investment will not be recovered over the service life. It is not appropriate, however, to transfer responsibility for recovery of this plant to Apollo under standard ratemaking practices. While Apollo might have compensated GTECA in the nonregulated context for its share of the investment not recovered by regulated depreciation rates, under tariff regulation such recovery is both non-standard and inappropriate.

Recovery of the investment adjustment from Apollo also is clearly incorrect. GTE stated that the \$1.3 million adjustment to gross investment was to eliminate certain assets "such that the resulting net book value transferred to regulated accounts reflects the usable portion of the facilities as well as the value of the broadband network..."¹⁶ The annuity payment represented by GTE's "nonrecoverable" cost is sufficient to recover this nonregulated investment adjustment as well as the undepreciated plant balance at the end of Apollo's service term. Customers of regulated services should not bear amounts that were not transferred to regulated accounts. Therefore, the "nonrecoverable" costs have been improperly allocated to Apollo. Recovery of these costs, if appropriate at all, must be the responsibility of the entity that benefited from abrogation of the GTE/Apollo contract, i.e., GTESC.

2. Administration costs. GTE's tariff support for annual "administration" costs is based upon an annual charge factor of 9.33%. This is substantially higher than GTECA's average administration expenses for 1993 and 1994. The factor fails to reflect the essentially passive nature of GTECA's role with respect to Apollo's channel allocation.

¹⁴ Transmittal 873, Exhibit B, p. 1.

¹⁵ ARMIS Report 43-02 (1994), Table B-7-1.

¹⁶ Transmittal 873, D&J, p. 8 emphasis added.

Analysis of GTE Telephone Companies' Cerritos Tariff Rates

We recalculated the administration charge factor based upon GTECA's average total company costs for 1993 and 1994 using data from ARMIS report 43-02. Only those accounts which were consistent with GTECA's essentially passive administrative role with respect to Apollo's 39 channels were included. These calculations are shown on Worksheet 2. The resulting charge factor is 7.48%

3. Maintenance costs. GTE's tariff support cost for annual "maintenance" costs is based upon an annual charge factor of 3.95%. While GTE might argue that some recovery of its maintenance costs from Apollo is appropriate, because when the contract was deemed to be abrogated, GTECA assumed certain maintenance responsibilities previously undertaken by Apollo.¹⁷ However, the factor used by GTE is substantially higher than GTECA's reported plant specific maintenance costs for 1993 and 1994 for the specific classes of plant in the Cerritos system (primarily underground cable and conduit). The plant specific average expense factor is developed on Worksheet 2. It is 1.15% per year instead of the 3.95% used by GTECA.

We examined other available GTE video transport capacity tariffs in order to verify that the annual charge factors applied by GTE to the Cerritos tariff were excessive. The annual charge factor used in Transmittals 873 and 874 exclusive of depreciation cost recovery, is 28.14%.¹⁸ Several different GTE operating companies recently tariffed a wholesale video transport service including a wholesale transport function analogous to the network transport component of the Cerritos system. As shown on Worksheet 4, the average annual charge factor exclusive of depreciation for these video transport offerings is only 14.89%. The charge factors are quite uniform across the various GTE LECs. Thus, the operating and return/tax charge for the Cerritos system is about 89% higher than these wholesale transport offerings. Unlike Apollo's 39-channel share of the Cerritos system, the GTE LECs still must incur and recover marketing and management costs with respect to the wholesale video transport service. Therefore, the cost data supporting the wholesale video channel offering confirm, again, that GTE has not used

¹⁷ Transmittal 873, D&J p. 5.

¹⁸ See Worksheet 1, line 39.

"standard" ratemaking factors with respect to the cost development for Transmittals 873 and 874.

Worksheet 3, attached, demonstrates the appropriate ratemaking calculation for Apollo under Transmittal 873, and shows the effect on GTE's rate if the added costs that were inappropriately included in the lump-sum charge under Transmittal 873 were recovered instead from GTESC — the very entity that benefits from the supposed abrogation of Apollo's contract. Instead of \$81,764, Apollo's appropriate monthly charge based upon standard ratemaking practice should be \$57,571.74. Apollo is owed a refund by GTECA of \$1,196,151 exclusive of any accrued interest. The corresponding tariff rate for GTESC should be set at \$94,422 per month in order to ensure that GTECA's other regulated activities do not bear any of the "costs" that GTE originally identified in the tariff filings. This monthly rate gives GTESC a pro rata credit for the excessive GTECA annual administration and maintenance costs associated with Transmittals 873 and 874. If the Commission determines that the total charges to Apollo and GTESC should still recover the annual costs identified by GTECA, then GTESC should pay \$105,956 per month. See Worksheet 3.

IV. Conclusion

GTE's claim that it is not discriminating between Apollo and its affiliate GTESC is based mainly upon the identity of the tariff charges applied to the two entities. This identity of charges is irrelevant, however, to the economics of the present Cerritos situation, in which Apollo stands merely as a customer of GTECA and GTESC stands as an affiliate of the LEC. Apollo's tariff rate should be calculated as that for a customer of GTECA, a customer whose own business activities eliminate most marketing and administration costs typically associated with GTECA's retail end user services. GTESC's rate should be calculated as that for an interested affiliate of GTECA, an affiliate which gained certain economic opportunities when the contract with Apollo was ostensibly abrogated. Therefore, GTESC should bear all of the residual risks of the project rather than sharing these costs with GTECA's customer, Apollo CableVision.

Summary of Worksheets

Worksheet 1 mainly replicates GTECA Exhibit B, p. 1 of 2 in Transmittals 873 and 874. Lines 39-41 compare the charge factors used by GTECA with the other charge factors used in GTE tariff filings.

Worksheet 2 develops comparable average charge factors from GTECA's ARMIS 43-02 reports.

Worksheet 3 recalculates the appropriate charges for Apollo and GTESC using the reduced administration and maintenance charge factors from Worksheet 2 and eliminating the so-called "non-recoverable" cost from Apollo's tarified charge. Lines 21-23 of Worksheet 3 are a comparison involving GTECA's annual charge factors for costs that are clearly not relevant to Apollo's 39 channels, including marketing and GTECA's other administration costs like procurement and research and development. This comparison shows that the actual charge factor applied to Apollo's portion of the system [23.2%, Worksheet 3, line 17] would closely equate to the charge factors that GTECA would utilize in an end user tariff filing for a service that it administered and marketed itself (unlike Apollo's service)

Worksheet 4 shows the development of the net charge factors, after depreciation, from other GTE companies' wholesale video service offerings, and shows that the comparable charge factor used in Transmittals 873 and 874 was considerably higher.

WORKSHEET 1

REPLICATION OF GTE COST ANALYSIS

INVESTMENT				
1	Buildings	\$7,232.09		
2	Furniture	\$1,286.16		
3	Analog Switching	\$20,747.37		
4	Circuit	\$809,023.93		
5	UG Metallic Cable	\$2,011,623.27		
6	Conduit	\$3,099,062.64		
7	Total Material	\$5,948,975.46		
8	Net Salvage Value	\$0.00		
9	Net Material Cost	\$5,948,975.46		
ANNUAL COSTS			GTE Percent of Net Mat'l Cost	
10	Building - Dep	\$212.71	0.00%	25
11	Furniture - Dep	\$91.80	0.00%	26
12	Switching - Dep	\$1,595.95	0.03%	27
13	Circuit - Dep.	\$80,903.29	1.36%	28
14	UG Cable - Dep.	\$143,687.38	2.42%	29
15	Conduit - Dep.	\$61,981.25	1.04%	30
16	Return	\$334,630.32	5.63%	31
17	F&S IT	\$214,498.03	3.61%	32
18	Annual "nonrecoverable"	\$303,784.03	5.11%	33
19	Administration	\$555,239.80	9.33%	34
20	Other	\$0.00	0.00%	35
21	Property Tax	\$30,711.41	0.52%	36
22	Maintenance	\$235,000.09	3.95%	37
23	Total Annual Cost	\$1,962,336.06	Charge factor	32.99% 38
24	Monthly cost	\$81,764.00	Charge Factor w/o Depreciation L38 - L25 to L30	28.14% 39
			Administration & Maintenance L33 + L37	13.28% 40
			Percent of Total	40.27% 41

WORKSHEET 2

AVERAGE GTECA COMPARABLE DATA AND CHARGE FACTORS

Comparable expenses as a percent of net plant

	1994	Percent of Net Plant	1993	Percent of Net Plant
1 Total Net Plant	4,674,843		4,798,684	
<i>Expenses Comparable to Apollo System</i>				
Land & Buildings Expense	62,733		60,431	
Furniture	6,019		5,176	
2 Subtotal	68,752	1.47%	65,607	1.37%
Analog Switching specific	4,824		4,554	
Circuit specific	22,034		21,873	
UG Cable specific	23,588		27,419	
Conduit specific	2,073		2,589	
3 Subtotal	52,519	1.12%	56,435	1.18%
Network Administration	47,126		54,900	
Plant Ops Administration	40,119		45,324	
4 Subtotal	87,245	1.87%	100,224	2.09%
5 Corp. Ops – Direct	203,091	4.34%	183,497	3.82%
Total Comparable factor		Average of 1993 & 94		
6 Administration Ls2,4 & 5		7.48%		
7 Maintenance L3		1.15%		
<i>Comparative Expense Factors</i>				
Total GS Expense	213,818	4.57%	195,095	4.07%
Total Plant Specific	504,254	10.79%	502,485	10.47%
Total Customer Ops	343,559	7.35%	334,102	6.96%

Source: GTECA Form 43-02, 1993 and 1994

**Overstated Administration and Maintenance
With Annual "nonrecoverable" expense eliminated**

Demonstration that addition of operating expenses would produce a reasonable charge factor:

21 Marketing	78,403	1.6%
22 Net Corporate operations [w/o R&D, Proc & Finance]	109,625	2.3%
23 Composite factor		27.1%

WORKSHEET 4
COMPARISON OF CERRITOS CHARGE FACTOR
WITHOUT DEPRECIATION TO
GTOC Wholesale Video Transport Service

1 Transmittal 873, 874 Total Charge
 factor without Depreciation 28.14%
 [Worksheet 1, L39]

GTOCs Rates for Wholesale Transport -- all years

State	MHz Capacity	Rate	Charge Factors w/o Depreciation
MI	40-450 MH	\$3,977.92	14.64%
MI	50-550 MH	\$4,222.88	14.92%
IL	40-450 MH	\$4,182.68	15.84%
IL	50-550 MH	\$4,260.12	15.88%
MN	40-450 MH	\$4,304.45	15.63%
MN	50-550 MH	\$4,382.17	15.70%
KY	40-450 MH	\$4,981.87	11.66%
KY	50-550 MH	\$5,065.35	11.71%
MO	40-450 MH	\$4,403.49	18.05%
MO	50-550 MH	\$4,480.02	17.65%
AR	40-450 MH	\$4,345.36	13.47%
AR	50-550 MH	\$4,225.59	13.56%

2 AVERAGE 14.88%

3 Transm. 873,874 difference 88.9% higher

Source:
GTOC & GTE STC -- Joint Tariff FCC 1
Transmittal #1, May 19, 1995

William Page Montgomery

William Page Montgomery, the Principal of Montgomery Consulting, has many years of experience studying a variety of economic and public policy areas affecting the telecommunications industry — including regulatory theory, cost and pricing issues, access services, and network management.

He has been directly involved in hundreds of public policy and rate matters before many state public utility commissions, and the Federal Communications Commission. He has conducted economic and policy studies for corporate, consumer and public sector clients including the International Communications Association, several state consumer advocates and other organizations. In 1993, he was co-recipient of the Industry Achievement Award from the ICA.

Mr. Montgomery has undertaken a variety of research projects for regulators in several jurisdictions, and has participated in projects undertaken for state consumer groups, attorneys general and other state agencies. These have included consulting assignments on behalf of the Connecticut Public Utilities Control Authority, the District of Columbia Public Service Commission, the Washington Utilities and Transportation Commission, the Minnesota Department of Public Service, the Kansas Corporation Commission, the Common Carrier Bureau, Federal Communications Commission and the Canadian Radio-television and Telecommunications Commission.

He has a J.D. degree from the Duke University School of Law; and a B.A., magna cum laude, in economics from Butler University. Previously, he was the Senior Vice President of Economics and Technology, Inc. for 16 years. From 1974-77 he was employed by the Regulatory Law Division of the U.S. General Services Administration in Washington, serving at the end of his tenure in the capacity of the chief counsel for telecommunications regulatory activities.

PARTICIPATION IN FCC, STATE AND OTHER REGULATORY MATTERS

FCC Docket or Other Matter	Subject Matter	FCC Docket or Other Matter	Subject Matter
78-72	MTS and WATS Market Structure	84-469	Revision of Uniform System of Accounts
79-106	Detariffing Installation Inside Wiring	84-800	Rates of Return for Interstate Services
79-245	Cost Allocation Manuals	84-1235	Guidelines for Dominant Carriers
79-246	AT&T Private Line Restructure		Optional Tariffs
80-286	Federal-State Joint Board Separations Investigation	85-	Annual 1985 Access Tariff Filings
80-765	AT&T WATS: Time of Day Rates	85-26	Furnishing CPE by Exchange Carriers
81-883	Deregulation of AT&T Customer Premises Equipment	85-88	Detariffing of Billing/Collection Services
83-426	Investigation of "Private Carrier" Status and Part 94	85-107	International Competitive Carrier Policy
83-1145	Investigation of Divestiture Related Tariffs	85-124	Feature Group A/B Access Service
83-1147	Long-run Regulation of AT&T	85-128	Investigation of AT&T PRO America Tariffs
84-369	Investigation of Special Construction Tariffs	85-166	Investigation of LEC Special Access Tariffs

William Page Montgomery

FCC Docket or Other Matter	Subject Matter	FCC Docket or Other Matter	Subject Matter
85-203	AT&T Revisions to Tariffs 1, 9, and 10 (SDN)	87-530	Investigation of Private Network Access
85-229	Computer Inquiry III (Phases I and II)	87-568	Investigation of AT&T Custom Services Tariffs
85-308	Amendments of Annual Form M & Report 901	87-811	Investigation of AT&T 1988 Tariff Revisions
85-326	AT&T Revisions to Tariffs 2, 9 and 10 (Megacom)	1987-88	Petitions Regarding FCC Network Jurisdiction
85-400	AT&T Revisions to Tariffs 9, 10, and 11 (private lines)	88-1	Investigation of Annual 1988 Access Tariffs
86-125	Midyear 1986 Access Tariff Filings	88-2	Review of Open Network Architecture
86-1	Revisions to Parts 67 and 69 of Rules	88-136	Investigation of Tariffs for DS3 Services
86-10	Provisions of 800 Service Number Portability (Phases I and II)	89-79	Investigation of Part 69 Rules for ONA and Other Services
86-79	Rules for BOC Marketing of CPE	89-824	Investigation of Rate of Return for Access Services
86-81	AT&T WATS Rates	NTIA	US Telecommunications Infrastructure Investigation
86-111	Amendment of Part 31 Accounting for Class A/B Companies	90-132	Regulation in Interexchange Services Market
86- (misc.)	Petitions for Waiver of Part 69 - NTS Costs	91-141	Expanded Special Access Interconnection of LEC Services
86-125	Phase I 1985 Access Tariff Filings	91-213	Local Access and Transport Pricing Investigation
86-182	Reporting Regulations for Tier 1 Carriers: (ARMIS)	92-13	Non-dominant Interexchange Carrier Tariff Filing Requirements
86-297	Amendment of Part 67 -- Separations Rules	92-91	Investigation of ONA Tariffs
86-421	Investigation of Dominant Carrier Deregulation	92-101	Investigation of Ratemaking Treatment of FAS 106
NTIA	Review of Rate of Return Regulation	92-222	Switched Access Interconnection of LEC Services
US v. AT&T	Triennial Review of BOC Business Restrictions	92-265	Cable Act Implementation / Program Access
86-497	Revisions to Rate Base Accounting Rules	92-266	Cable Act Implementation / Rate Regulation
86-423	Revised Line Power Requirements for DS1 Services	93-22	Implementation of Telephone Disclosure and Dispute Resolution Act
80-286	Joint Board Investigation of COE Separations (1987)	93-215	Cable Act Implementation / Cost of Service
87-113	1988 Access Charge Rule Changes	93-251	Modifications of Cost Accounting Rules
US v. AT&T	Review of BOC Provision of Switching Services	93-252	Investigation of Telecommunications Fraud
87-215	Investigation of Access for Information Services	94-1	LEC Price Cap Performance Review
87-313	Regulatory Reform for Dominant Carriers (Price Caps)	94-102	Compatibility Rules for Enhanced 9-1-1 Service
87-447	Amortization of Depreciation Reserve Deficiency		
87-469	Rescription of the Authorized Rates of Return		

William Page Montgomery

State Proceedings since 1981			
<u>Date of Submission</u>	<u>State Regulatory Commission</u>		
		November 1994	Commission
		January 1995	Iowa Board of Public Utilities
			Utah Public Service
			Commission
November 1981	Illinois Commerce Commission	March 1995	Oregon Public Utilities
December 1981	Kansas SCC		Commission
April 1982	Wisconsin Public Service	April 1995	Washington Utilities and
	Commission		Transportation Commission
August 1982	Kansas SCC	May 1995	Maryland PSC
October 1982	Public Utilities Commission of		
	Ohio		
November 1982	New York Public Service		
	Commission		
March 1983	Wisconsin PSC		
June 1983	California PUC		
August 1983	California PUC		
October 1983	Kansas State Corp. Commission		
November 1983	California PUC		
December 1983	California PUC		
December 1983	Texas PUC		
June 1984	New York PSC		
October 1985	Texas PUC		
January 1986	California PUC		
February 1986	Texas PUC		
February 1986	California PUC		
May 1989	Illinois Commerce Commission		
May 1989	Connecticut Department of		
	Public Utility Control		
July 1989	Illinois Commerce Commission		
February 1990	South Carolina Public Service		
	Commission		
March 1990	Connecticut DPUC		
September 1990	Florida Public Service		
	Commission		
November 1990	Louisiana Public Service		
	Commission		
April 1991	Connecticut DPUC		
September 1991	Colorado Public Utilities		
	Commission		
March 1992	Florida PSC		
October 1992	Connecticut DPUC		
May 1993	Connecticut DPUC		
January 1994	Maryland Public Service		
	Commission		
June 1994	Washington Utility and		
	Transportation Commission		
August 1994	Illinois Commerce Commission		
October 1994	Texas PUC		
October 1994	Washington Utility and		
	Transportation Commission		
November 1994	Pennsylvania Public Utilities		

GTE California Incorporated
CABLE TELEVISION WORK ORDER
 FORM CA 1355

95205 GTE

DISTRIBUTION:
 White - Originator Retains
 Yellow - Apollo Cable Television
 Pink - Service Corp.
 Blue - Customer

COMMITMENT INFORMATION		
DUE DATE 7-22-95	COMMIT TIME AM 1 10	ACCESS: All Day or Between _____ and _____

CUSTOMER INFORMATION	
CUSTOMER NAME DUANE EVANS	ACCOUNT NUMBER 113158-1
CUSTOMER ADDRESS 17609 S. ERIC AVE	
CUSTOMER PHONE NUMBER 865-6787	CBR NO TAG #
SPECIAL ACCESS ARRANGEMENTS	

WORK REQUESTED / COMPLETED	
INSTALLATION REQUEST:	
INSTALLATION COMPLETED: <input type="checkbox"/> RECONNECT OR <input type="checkbox"/> NEW DROP INSTALLED	
NUMBER OF CONVERTERS INSTALLED	NUMBER OF REMOTES
CONVERTER NO'S 10199064 ()	10122829 ()
TIMING'S Connected to phone network: <input type="checkbox"/> Y or N	<input type="checkbox"/> Y or N
INTERIOR WIRE INSTALLED AND/OR ANCILLARY EQUIPMENT CONNECTED	
FIRST LOCATION MINUTES	ADDITIONAL LOCATIONS MINUTES*
TROUBLE REPORTED: BAD BOX CRR1 CHECK MURKIN	
TROUBLE FOUND: SUB HAS HAD SIGNAL BARS IN PAST FEW MONTHS CHECKED SIGNAL/TALK 2K.	

SIGNAL READING	LOW	MEDIUM	HIGH	SUPER	TECHNICIAN NAME
Converter					COREY
Top Signal					TECHNICIAN NO.:

WORK ORDER STATUS	
VISIT TIME 7:35	COMMIT TIME 12:40
COMMIT MET: <input checked="" type="checkbox"/> YES OR <input type="checkbox"/> NO	
<input checked="" type="checkbox"/> COMPLETED	<input type="checkbox"/> PARTIAL COMPLETION
<input checked="" type="checkbox"/> NO ACCESS	<input type="checkbox"/> CANCEL
<input type="checkbox"/> RESCHEDULE	
COMMENTS: NEED TO TALK TO JAHU MAYBE NEED TO RE WIRE BUTLET.	

CUSTOMER ACCEPTANCE	
I agree to the terms and conditions on the back of this document, and the GTE charges as noted.	Total GTE Charge
Customer Signature: _____ Date: 7-22-95	\$ (To be billed)

NEED TO TALK TO JAHU